

**IB ECONOMICS – INTERNAL ASSESSMENT SUMMARY PORTFOLIO  
COVERSHEET**

School Code:  003542	Name of School:  Nagoya International School
Candidate Number:  003542-0014	Candidate Name:  Yuna Suzuki

Commentary Number	Date Article Published	Date Commentary Written	Different and Appropriate Source	Section of the Syllabus that the Article relates to	Number of Words
1	April 25, 2013	May 28, 2013	BBC News BUSINESS	Macroeconomics	750
2	November 20, 2013	January 19, 2014	Bangkok Post	International Economics	749
3	February 15, 2014	March 12, 2014	Manila Times	Development Economics	749

IB Economics – Internal Assessment Coversheet  
For May 2014

School Code	003542
Name of School	Nagoya International School
Candidate name	Yuna Suzuki
Candidate number	003542-0014
Teacher	Paul Jacobsen
Title of the Article	Abenomics: Can it really end deflation in Japan?
Source of the Article	BBC News BUSINESS <a href="http://www.bbc.com/news/business-22299450">http://www.bbc.com/news/business-22299450</a>
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Section of the syllabus that the article relates to. [Please check the section that is the most relevant.]	<p>Section 1: Microeconomics _____</p> <p>Section 2: Macroeconomics <u>  √  </u></p> <p>Section 3: International Economics _____</p> <p>Section 4 : Development Economics _____</p>

Article Title: Abenomics: Can it really end deflation in Japan?  
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Article Published: April 25 2013  
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Relation to Syllabus: Deflation and Expansionary Fiscal (Monetary) Policy  
**25 April 2013** Last updated at 21:22 GMT

Yuna Suzuki 11  
Economics (SL) IA

### **Abenomics: Can it really end deflation in Japan?**

**The Bank of Japan is undertaking one of the most aggressive injections of cash by any central bank in the world in order to try to combat falling prices and achieve 2% inflation in 2 years.**

The central bank, which holds its latest policy-making meeting on Friday, plans to expand its balance sheet to 270 trillion yen (\$2.8tn; £1.8tn) by the end of 2014. This equates to about 53% of GDP or economic output in that year.

The policy is part of a bold new set of economic measures backed by Japan's Prime Minister, Shinzo Abe, known as Abenomics.

Declining prices of goods and services - deflation - discourages consumers from making purchases because they expect prices to be lower in the future.

It is a vicious cycle - as consumers delay purchases, businesses see demand fall so they postpone investment. It has contributed to a stagnant economy in Japan since the property crash in the early 1990s.

The question now is will it work? If there are three yen instead of two yen chasing each good or service produced, then surely that will raise prices?

#### **'Bazooka'**

It is not the first time that it has been tried. In 1997, the BOJ balance sheet was 50 trillion yen. It grew to three times that size a decade later and yet deflation persisted.

Deflation did cease at times, but a lack of demand for credit meant that money still was not flowing in the economy, so deflation returned once the BOJ halted its cash injections.

What is different this time? The BOJ is unlikely to end its injections prematurely since the Finance Minister Taro Aso calls the policy a "bazooka".

The government is also increasing spending to try to raise GDP by 2%. This boost to demand is designed to encourage firms to invest rather than hoard cash, another important part of ending the deflationary cycle.

There are some promising signs.

A key indicator is how consumers react. The Japanese Cabinet Office's consumer sentiment survey from last month found that nearly three quarters (71.8%) of households expect prices to rise over the next 12 months.

If consumers expect prices to rise, then they will not put off purchases and could break the vicious cycle. The IMF seems to think they will, as it estimates that inflation will be 3% in 2014, a figure that has not been seen since the real estate bubble burst more than two decades ago.

**Wider implications?**

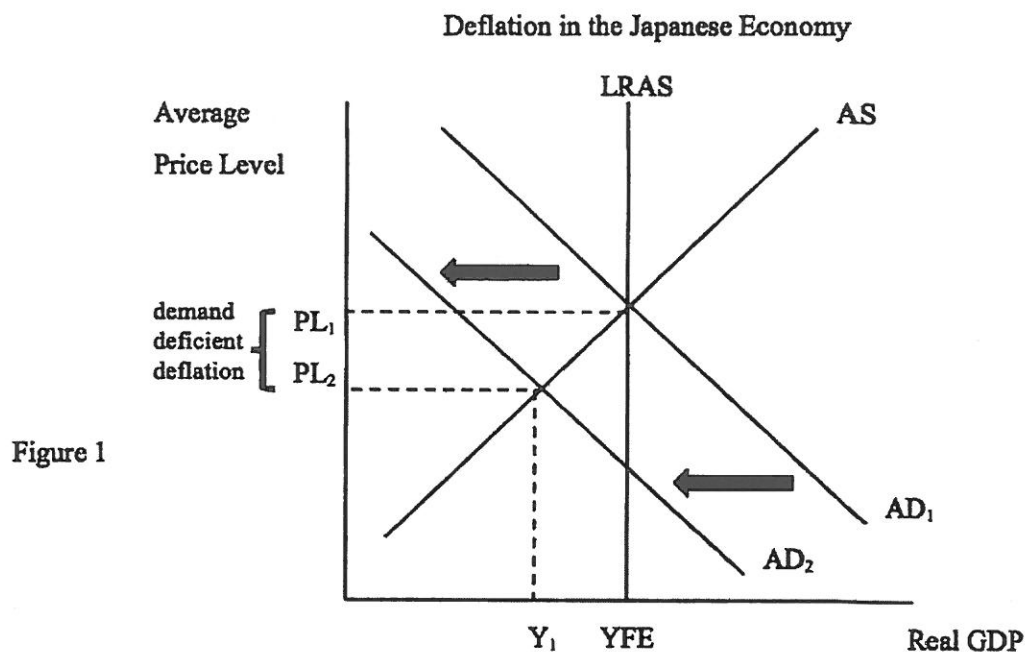
If Japan's massive stimulus succeeds in ending deflation, it could have an impact on monetary policy far beyond the country.

Other central banks, including the US and UK, have been running major quantitative easing (QE) programmes for a number of years, injecting billions of dollars into their financial systems to try to kick start growth.

So if Prime Minister Abe's QE succeeds, and it does so through changing the inflation expectations of consumers, it will be proof of how inflationary the policy can be.

That is good news for Japan after more than a decade of falling prices. But it may not be so good for other countries who face rising, not declining prices.

This article is concerned with Japan's long-lasting deflation. Japan is in deflation since the early 1990's when the economic bubble burst. Deflation is a decrease in the average price level.



The graph above represents the current situation Japan is facing—demand-deficient deflation. Before deflation occurred in the 1990s, we assume the real GDP was at  $Y_{FE}$ . However as the economic bubble burst, Japan plunged into decades of deflation where average price levels of goods and services continued to stay low. This is explained in the article as a result of consumers being discouraged from making purchases because they expect prices to be lower in the future. This ‘change in consumer confidence’ effects consumption, as it is a factor of AD. Thus the discouragement of consumers from making purchases affects AD by decreasing it from  $AD_1$  to  $AD_2$ , decreasing the average price level of all goods and services from  $PL_1$  to  $PL_2$ . This creates a deflationary gap as seen in the gap between  $Y_{FE}$  and  $Y_1$ . However this situation has been dragging in Japan for the past 20 years, thus generating a deflationary spiral, where AD continues to fall while the deflationary pressure builds. This cycle is caused due to a decrease in consumption and investment, contributing to the stagnant economy in Japan since the crash in the 1990s.

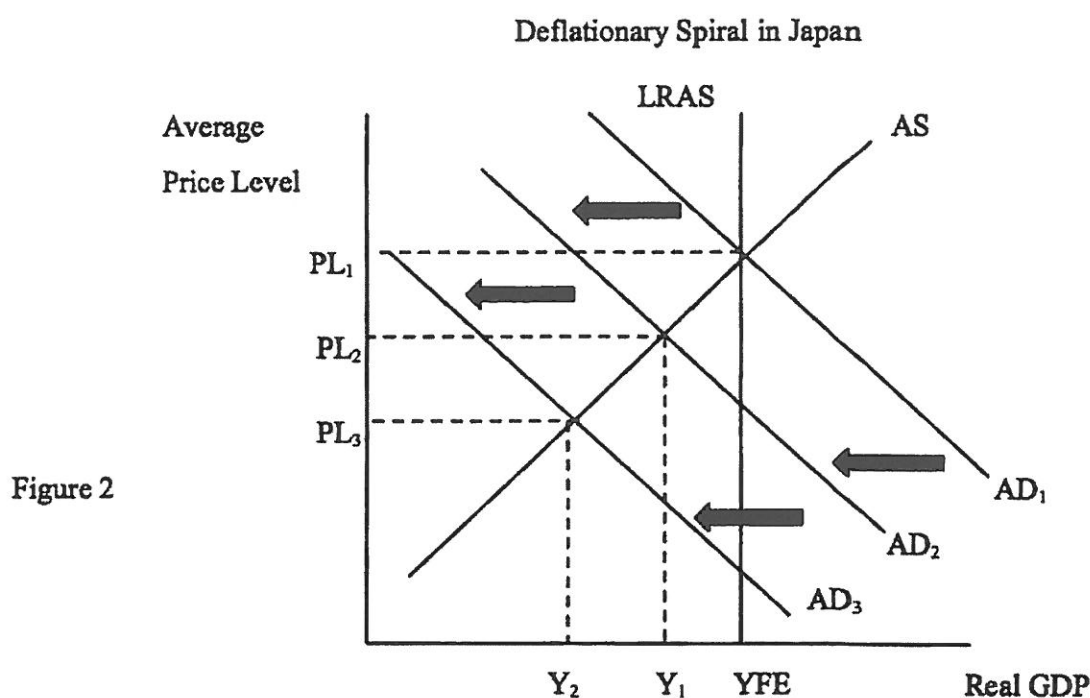
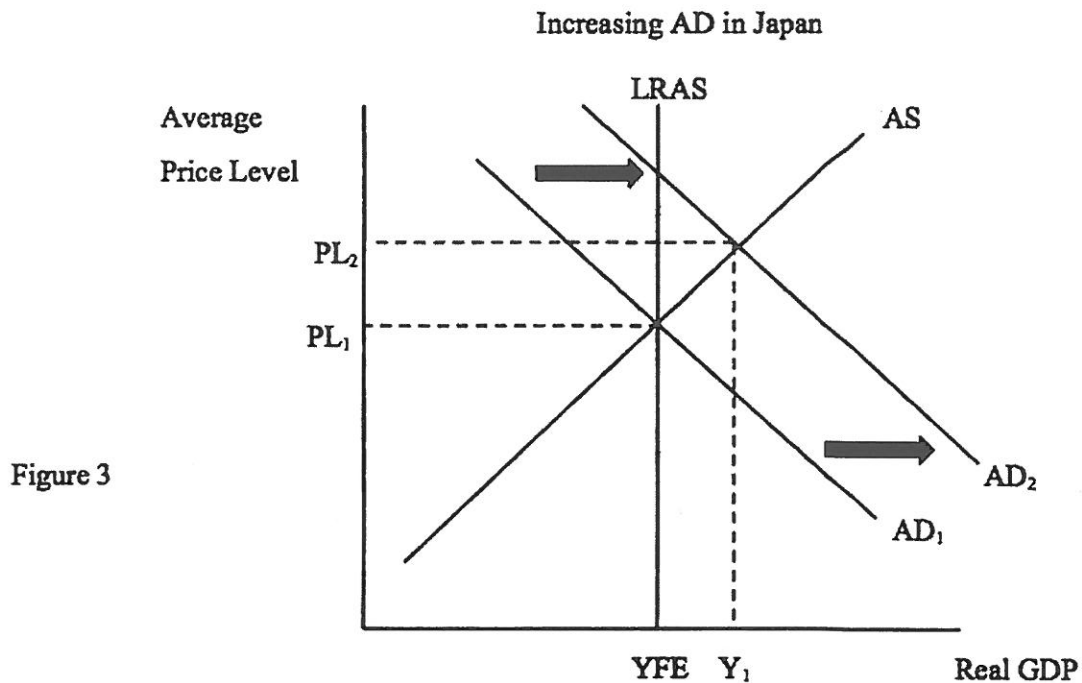


Figure 2

The graph above displays the deflationary spiral Japan is in since the 1990s. We assume that the economy was at YFE. The expectation of future falling prices creates an incentive for Japanese consumers to delay purchases and firms to invest less, causing a decrease in AD from AD<sub>1</sub> to AD<sub>2</sub>, as both consumption and investment are factors of AD. This decrease in AD is demand-deficient deflation as the average price level for all goods and services in Japan lowered from PL<sub>1</sub> to PL<sub>2</sub>, discouraging consumption and investment. As AD fell to AD<sub>1</sub>, unemployment increased as shown by the drop from YFE to Y<sub>1</sub>. With households having less disposable income, consumers consumed less, causing AD to fall from AD<sub>2</sub> to AD<sub>3</sub>. The continuation of AD falling created a deflationary spiral in the Japanese economy. Japan has plunged into this cycle for approximately two decades and the article claims that by injecting 270 trillion yen by the end of 2014, Japan is aiming to achieve 2% inflation.



As a solution, Prime Minister Abe decided to implement fiscal policies called 'Abenomics' by increasing government expenditure. Knowing that government expenditure is a component of AD, it is expected that an increase in government spending will increase AD. The government is also aiming to increase corporate confidence in order to encourage investment. Investment is also a component of AD, thus an increase in both consumption and investment should shift AD from  $AD_1$  to  $AD_2$ , as seen in Figure 3. Additionally, as 71.8% of households expect prices to rise over the next 12 months, they will begin to increase consumption, which will also contribute to increase AD. If Abe does achieve to increase government expenditure, investment, and consumption, then the article states that Japan will be able to break the deflationary spiral she was trapped in for decades.

Though it is anticipated that Abenomics would stimulate inflation and economic growth in Japan, there are possible disadvantages to expansionary fiscal policies. Time lag is always crucial, specifically recognition and impact lags. A recognition lag is the time for policy makers to recognize a problem is happening, while an impact lag is the time for a policy to affect the economy. Policies take 6-18 months to be enacted, thus if the policy impacts during a recovery period, then it may have negative impacts such as excessive inflation. We are never sure of where the economy is on a graph, thus when to implement policies is crucial yet difficult to assess. Also the amount of money to inject into the economy is highly difficult to calculate, as it is hard to measure the money supply in the economy.

Even with these disadvantages, expansionary fiscal policies is the best solution to the

demand-deficient deflation Japan is facing. If the Japanese government increases government expenditure and decreases taxes, AD should shift from  $AD_1$  to  $AD_2$  in Figure 1. While fiscal policies focus on increasing consumption by increasing government expenditure and cutting taxes, monetary policies focus on investment. Monetary policies can alleviate demand-deficient deflation by decreasing the interest rate, thus encouraging investment; a factor of AD. Both fiscal and monetary policies are favourable to use during recessions, thus the best solution to Japan's problem is to implement both types of policies. They will increase AD by stimulating investment, consumption and government expenditure, creating inflation within the Japanese economy, combatting the 20 year long deflation.



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School Code	003542
Name of School	Nagoya International School
Candidate name	Yuna Suzuki
Candidate number	003542-0014
Teacher	Paul Jacobsen
Title of the Article	New Zealand keen on Thai trade hub
Source of the Article	Bangkok Post <a href="http://www.bangkokpost.com/business/news/380721/new-zealand-keen-on-thai-trade-hub">http://www.bangkokpost.com/business/news/380721/new-zealand-keen-on-thai-trade-hub</a>
Date the Article was published	November 20, 2013
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**Record: 1****Title:**New Zealand keen on Thai trade hub**Authors:**Wiriyapong, Nareerat**Source:**Bangkok Post (Thailand). 11/20/2013.**Document Type:**Article**Accession Number:**2W62367276418**Database:**Newspaper Source**New Zealand keen on Thai trade hub**

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Nareerat Wiriyapong

Nov. 20--Thailand's geographical advantages prompted New Zealand firms to consider expanding their presence to Southeast Asia using Thailand as a regional hub, says New Zealand Prime Minister John Key.

In an interview with the Bangkok Post, Mr Key said a broad range of opportunities are available in Thailand and neighbouring countries, including Cambodia and Laos. Myanmar has gone through rapid reforms and New Zealand recently changed its position towards the country.

For example, law firms in New Zealand are looking at business opportunities in Myanmar through a Bangkok base, he said.

My Key is leading a delegation of 22 companies to Thailand for a bilateral visit from Nov 17-20 following a trip by Prime Minister Yingluck Shinawatra to New Zealand a month ago.

"Thailand has geographical advantages with developed infrastructures, and is a democratic country with predictability and a legal system," he said.

With 57 years of bilateral relations, Thailand and New Zealand have two free-trade agreements (FTA) including the Thai-New Zealand Closer Economic Partnership (CEP) signed in 2005. The Asean-Australia-New Zealand FTA came into effect in 2010.

Trade in goods has nearly doubled since the signing of the CEP, reaching NZ\$2.17 billion in the first six months of this year from NZ\$1.67 billion for all of 2005. In March, the two leaders vowed to double bilateral trade by 2020.

Exports from Thailand to New Zealand totalled NZ\$1.54 billion in the first half of this year, nearly double from NZ\$819 million in 2005, consisting of mainly vehicles, polymers, and air conditioners. Over 90% of Thai products entering New Zealand are subject to CEP privileges or enter duty-free.

New Zealand's exports to Thailand amounted to NZ\$632 million, half of which are daily-use products, followed by wood products, apples and seafood.

In fiscal year 2012 ending in March, New Zealand investments in Thailand totalled NZ\$29 million.

Mr Key said the food and beverage, information technology and education sectors are considered high potential for New Zealand investors considering setting up here.

Orion Health already announced a partnership with Bumrungrad Hospital to expand its presence in the eHealth market in Southeast Asia.

Global logistics company Mainfreight plans to open its first Thailand office for its air and sea network in response to requests from its multinational customers to set up a presence in the region. Chief executive and managing director Don Braid said Thailand is a natural choice for its initial expansion in Asean.

"Thailand is perfectly positioned to provide intra-Asia trade growth, as well as facilitate existing trade within the Mainfreight network. We see Thailand as a leading economy in the 2015 Asean Economic Community," he said.

Mainfreight expects to double the size of its Bangkok office in the first year of operation to handle in excess of 3,000 shipments annually, said Mr Braid.

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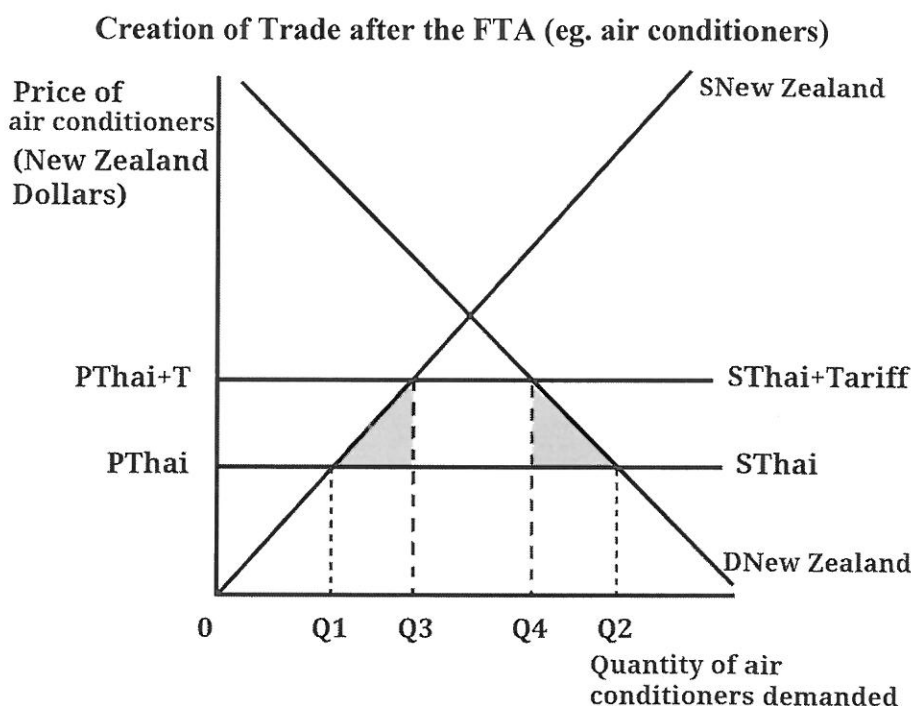
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**Source:** Bangkok Post (Thailand), Nov 20, 2013

**Item:** 2W62367276418

This article is concerned how New Zealand is seeking to expand into Southeast Asia by forming the "...Thai-New Zealand Closer Economic Partnership (CEP), a free trade agreement (FTA)." An FTA is formed by two or more nations who make an agreement to completely eliminate tariffs on most goods and services produced in and imported from all other member states.<sup>1</sup> Such trading blocs are formed by countries in order to approach a truer form of free trade.

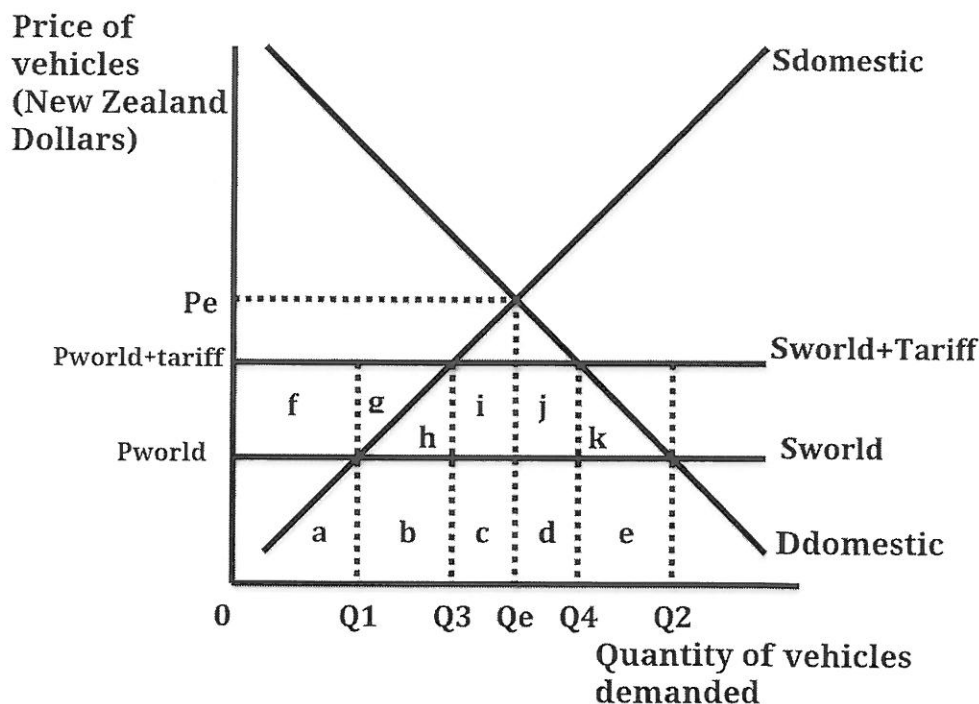


Before New Zealand and Thailand formed the CEP FTA, New Zealand imported  $S_{\text{Thai}+\text{Tariff}}$  Thai air conditioners at price  $P_{\text{Thai}+T}$ . Here, the trade barrier protected domestic New Zealand air conditioner producers, as they were able to produce  $0 \sim Q_3$  at the higher price. However the formation of the FTA eliminated tariffs on "Over 90% of Thai products entering New Zealand...", lowering the price from  $P_{\text{Thai}+T}$  to  $P_{\text{Thai}}$ , and increasing supply of Thai air conditioners from  $Q_3 \sim Q_4$ , to  $Q_1 \sim Q_2$ , where the triangles shaded represent the regained world efficiency and consumer surplus. As reported by the article, export revenue increased from NZ\$819 million to NZ\$1.54 billion after the formation of the FTA, as a result of eliminating tariffs. This indicates that Thailand has the comparative advantage in producing air conditioners, as the increase in total revenue suggests trade creation; where "The entry of a country into a customs union leads to the production of a good or service transferring from a high-cost producer to a low-cost producer".<sup>2</sup> Trade is created as the more efficient producer, Thailand can now make full use of her comparative advantage in air conditioner making.

#### Eliminating Tariff on Thai imports

<sup>1</sup> Maley, Sean, and Jason Welker. "Trading Blocs." *Economics*. Oxford: Pearson Education, 2011. 511. Print.

<sup>2</sup> BLINK AND DORTON.



As stated in the article, “...over 90% of Thai products enter New Zealand duty-free”, meaning that tariffs are completely eliminated on those goods and services as a result of the FTA. A tariff is a tax charged on imported goods, thus are viewed as an added cost of production by firms, shifting the supply curve up.<sup>3</sup> A decrease in the cost of production leads to improved efficiency, which is one of the results of forming a FTA. Before the FTA was into effect, New Zealand produced 0~Q3 vehicles at  $P_{\text{world}+\text{tariff}}$ , while she imported Q3~Q4 vehicles. However with the FTA, prices decreased from  $P_{\text{world}+\text{tariff}}$  to  $P_{\text{world}}$ , where New Zealand produces from 0~Q1 vehicles, and imports Q1~Q2 vehicles from Thailand. With the elimination of tariffs on imported goods and services, Thailand increased her vehicle exports to New Zealand from Q3~Q4, to Q1~Q2, which can now be produced at the lower price level of  $P_{\text{world}}$ .

The article states, “Thailand’s geographical advantages [such as being located in Southeast Asia] prompted New Zealand..” to form this FTA, since she wanted to expand into the region. Though the revenue the New Zealand government loses accumulates in the long-term, the increase in export revenue the country experiences due to the FTA outweighs the losses the government undergoes. This may also lead to trade imbalances in the long-term, as currently Thailand’s exports total NZ\$1.54 billion, while New Zealand’s exports only total NZ\$632 million. This may be disadvantageous for New Zealand, as she is importing more than twice as much as she exports; a situation of current account deficit.

Once New Zealand goods and services enter Thailand, they can travel to other countries Thailand is in a trading bloc with; a long-term advantage which also applies to

<sup>3</sup> Maley, Sean, and Jason Welker. "Types of protectionism." *Economics*. Oxford: Pearson Education, 2011. 439. Print.

Thailand. As in the article, “New Zealand law firms are looking at business opportunities in Myanmar”, and as Thailand is a part of ASEAN, where she has relations with Cambodia, Laos, and Myanmar, forming the FTA was advantageous to New Zealand as it enabled her goods and services to flow to ASEAN member states, via Thailand. Once trade becomes more prevalent between New Zealand and Thailand, in the long-run, they may expand this FTA by either evolving it to a customs union, or augment the size of the FTA.

Forming the FTA was also advantageous on a wider scale, as it efficiently allocates scarce resources within member nations, based on their comparative advantage. This is done by reallocating resources such as steel in vehicle production to the more efficient Thai producers than the relatively inefficient New Zealand producers. Yet globally, creating an FTA may still be considered a misallocation of resources, as it completely eliminates tariffs on all goods and services only within the member countries, thus blocks non-member countries even if they have the comparative advantage in vehicle making.

## IB Economics—internal assessment coversheet

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| School code<br>003542 | Name of school<br>Nagoya International School |
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|--------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Candidate name                                                                             | Yuna Suzuki                                                                                                                                                                                                                                     |
| Candidate number                                                                           | 003542-0014                                                                                                                                                                                                                                     |
| Teacher                                                                                    | Paul Jacobsen                                                                                                                                                                                                                                   |
| Title of the article                                                                       | ADB extends \$250-M loan for LGC review                                                                                                                                                                                                         |
| Source of the article                                                                      | Manila Times, The (Philippines)<br><br>http://web.b.ebscohost.com/src/detail?<br>sid=0bec9ddfH7166H4ac0H90adH1cb2453f206e<br>%40sessionmgr115&vid=1&hid=120&bdata=JnNpd<br>GU9c3JjLWxpdmU %3d#db=ndh&AN=2W62558622470                           |
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| Section of the syllabus the article relates to (please tick the one that is most relevant) | <input type="checkbox"/> Section 1: Microeconomics<br><input type="checkbox"/> Section 2: Macroeconomics<br><input type="checkbox"/> Section 3: International economics<br><input checked="" type="checkbox"/> Section 4: Development economics |



**Record: 1****Title:**ADB extends \$250-M loan for LGC review**Authors:**Lazo, Kristyn Nika M.**Source:**Manila Times, The (Philippines). 02/15/2014.**Document Type:**Article**Accession Number:**2W62558622470**Database:**Newspaper Source**ADB extends \$250-M loan for LGC review**

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Kristyn Nika M. Lazo

Feb. 15--The Asian Development Bank (ADB) has approved a \$250-million loan to support the review of the country's Local Government Code (LGC) centering on "finance and fiscal decentralization reforms" in the Philippines.

Aside from the \$250-million loan by ADB, the LGC review would also be co-financed by France-based development group Agence Française de Développement with a \$150-million fund.

Juan Luis Gomez, ADB senior public management specialist for Southeast Asia, said in a statement that the \$250-million loan would provide support to the national government in the revision of the LGC, which would improve fiscal processes and handling in the country.

"The Philippines has taken significant steps to improve the financing system of local government units [LGUs], and to foster transparent and accountable local governance practices. Reforms should help raise revenues and therefore improve services," he added.

The LGC revisit would be the first since its enactment in 1991. The \$250-million loan would also be ADB's first to the Philippines for the year. The bank offered up to \$1 billion to the country last year because of the assistance needed for the rebuilding of areas hit by Super Typhoon Yolanda.

According to the ADB, the LGC review should be able to address the problem of "weak local tax bases" as well as the "flaws in the design of transfers" between local governments that result in lower efficiency the delivery of government services.

"Despite these efforts, weak local tax bases and flaws in the design of transfers make it hard for poorer local governments to deliver the services their constituencies require. As a result, regional disparities in living standards remain wide. This could be efficiently addressed with a review of the [LGC]," the ADB said.

Other reforms lined up for LGC include performance-based mechanisms such as the Performance Challenge Fund and the Bottom-up Budget that can "improve budget transparency and alignment of national and local development priorities."

The multilateral agency said that it supports the revision of the LGC as LGUs represent 17 percent of yearly government expenditures, which greatly contribute to different sectors such as health, education, and housing and community development.

"Program reforms will also continue implementation of accountability mechanisms, such as the Full Disclosure Policy or the Citizen's Satisfaction Index. Lastly, the program supports the government's efforts to improve local financial management systems," the ADB said.



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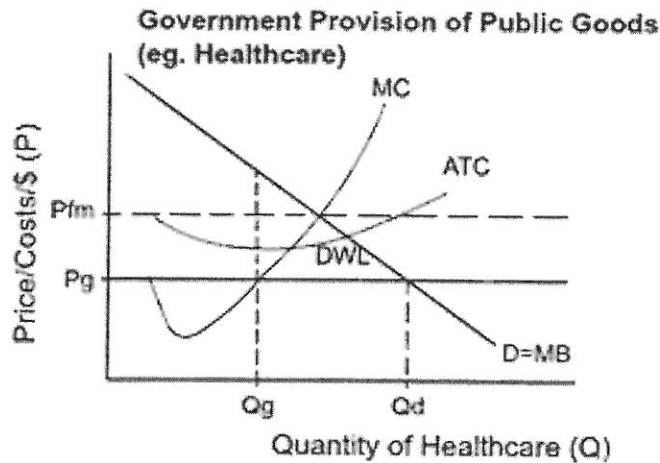
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**Source:** Manila Times, The (Philippines), Feb 15, 2014

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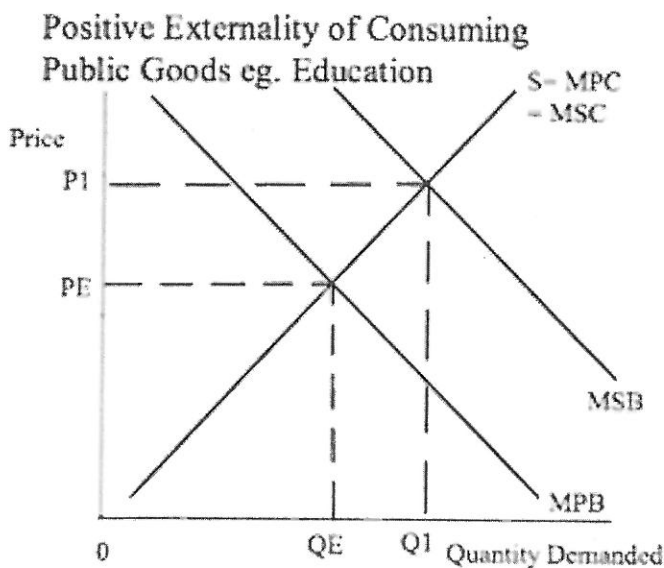
This article is concerning how the \$250-million loan by the Asian Development Bank is used to help the Philippine government review its Local Government Code on the country's fiscal processes. A loan is a sum of money which must be paid back with interest.<sup>1</sup>



The article states that the review of the LGC will aid the local government units by increasing the efficiency of delivery services. These units consist 17% of the total expenditure by the Filipino government, thus making the transactions between these units more efficient leads to an increase in government expenditure, as the government will have relatively more revenue to spend on public goods such as healthcare and education. The provision of such goods by the Filipino government can be modeled by the graph labelled Government Provision of Public Goods (eg. Healthcare), where healthcare is publicly funded at an affordable price to all citizens.<sup>2</sup>

Under a free market system,  $Q_m$  (a point between  $Q_g$  and  $Q_d$ ) would have been provided at price  $P_m$ , creating a market equilibrium. However since the government promotes equity in to break free from the poverty cycle her country is in, the government must force down the price to  $P_g$  for affordable healthcare to all Filipinos. This results in a situation of excess demand, where  $Q_d$  is demanded, yet the demands of only  $Q_g$  is met at the lower price of  $P_g$  due to the lack of resources. The under provision of public goods is represented by the gap between  $Q_d$  and  $Q_g$ , or the triangle of dead weight loss. This is highly inefficient, as large scale subsidies are necessary to sustain the low price of  $P_g$ . Additionally at  $Q_g, P_g$  where government provision of public goods establish an equilibrium,  $ATC$  is greater than  $MC$ , meaning that the cost of healthcare exceeds the price; creating economic losses.

Public goods are non-rivalrous and non-excludable goods, not provided by the market. Although it has a positive externality upon those who consume the goods and services, it is under provided as consumers do not realize the full benefits of the product. A positive externality of consumption occurs when a third party enjoys the benefits of the consumption of a good or service at where the marginal social benefit is greater than the marginal personal benefit. In a free market,



education would have been provided at  $Q_e$ , price  $P_e$ . However its optimum lies at  $Q_1, P_1$ , as the true societal value is higher than what it currently is, since its full benefits are not realized. An increase of government expenditure in public goods will help improve human capital, thus this loan can help provide more goods with positive externalities for the Filipinos. Theoretically, an increase in government expenditure and improved human capital leads to growth, due to an increase in AD and improved human capital, thus help break the poverty cycle. The loan supports the review of the LGC, which intends to improve services and raise government revenues to increase supply of public goods and positive spillovers.

<sup>1</sup> "Loan." Dictionary.com. Dictionary.com, n.d. Web. 11 Mar. 2014.

<sup>2</sup> Maley, Sean, and Jason Welker. "The Balance Between Markets and Intervention." Economics. Oxford: Pearson Education, 2011. 619-21. Print.

Improving the productivity via the injection of money may potentially break the poverty cycle, as low productivity is a component contributing to this cycle. Low productivity leads to low income as workers can only produce little output relative to the inputs. With less income, it is difficult to save due to less disposable income. Without savings, we cannot invest into human and natural resources to increase productivity; leading back to low productivity, repeating and perpetuating the cycle. Without aid, the article states that the living standards will remain wide due to inefficient transfers and weak tax bases. However, the problems the aid should address, such as raising revenues and improving services, were all stated by the ADB, a multilateral agency. This suggests that the aid was administered according to the goals and aims of the ADB in their point of view, thus this aid may not help the Philippines to truly break away from her poverty cycle. Additionally, the use of aid may be disadvantageous as they are highly inefficient, due to the deadweight loss it generates. Since the government can only provide public goods at the affordable lower price by subsidizing it, the subsidies used to help maintain low prices are an opportunity cost as it could have been spent on the next best good.